International Journal of Accounting and Financial Management Research (IJAFMR)
ISSN (P): 2249-6882; ISSN (E): 2249-7994
Vol. 8, Issue 4, Oct 2018, 17-26

THE RELATIONSHIP BETWEEN BOARD INDEPENDENCE AND FINANCIAL REPORTING QUALITY IN SAUDI NON-FINANCIAL LISTED FIRMS

MOHAMMED ALSHETWI

Associate Professor, Department of Accounting, College of Business & Economics, Qassim University, Buraidah, Saudi Arabia

ABSTRACT

This study examines the relationship between independent boards and Financial Reporting Quality (FRQ) of non-financial listed firms in Saudi Arabia. The current study uses abnormal accrual to measure FRQ. Alternatively, earnings persistence is used to enhance the validity of the study. The logit model is also used as an additional test to test the endogeneity problem. Using a sample of 417 firms in the period of 2013-2016, this study found that the presence of an independent board is not related to improve FRQ of non-financial listed firms in Saudi Arabia. This result is consistent with the view that the corporate governance system works differently in an environment with structural and organizational biases, such as when firms are controlled by CEOs and top management.

KEYWORDS: Independent Board, Financial Reporting Quality (FRQ), Non-Financial Listed Firms & Corporate Governance

Received: Aug 16, 2018; **Accepted:** Sep 06, 2018; **Published:** Sep 20, 2018; **Paper Id.:** IJAFMROCT20183

Original Article

INTRODUCTION

The financial reporting has an important role in the Organizational Governance. Based on the reliable and relevant information, an investor can make a good prediction regarding the firm's earnings. In recent years, financial reporting has been the focus of professional bodies due to its importance in building the investors' trust and enhancing the efficiency of capital markets. One of the mechanisms used by professional bodies to enhance the quality of their financial reporting systems is Corporate Governance (CG). CG is a set of tools adopted by the professional bodies to protect the interest of the shareholders and to build investors' confidence in the financial reporting.

The board of directors, among other CG tools, has an effective role in reducing agency conflict that might occur between management and shareholders. The board of directors has two main functions in an organization: it plays a vital role in setting the strategic direction of the organization; in addition, it is responsible for monitoring the financial reporting process. As required by CG rules, the board of directors should carry out the monitoring function that ensures the effectiveness of internal control and the integrity of financial reporting (CMA, 2006).

To fulfill these responsibilities, the board should implement certain procedures that ensure accountability and the monitoring of top management (Fama and Jensen, 1983), and overview the accounting practices and maintain the quality of financial reporting (Vafeas, 2000). In this regard, the board is authorized to nominate the

top management, approve its rewards, and dismiss it if necessary (Adams, Hermalin, and Weisbach, 2010). In addition, the board should ensure that the internal control system work properly (Jensen, 1993) and therefore, prevent irregularities and reduce fraud in the financial statement. In short, the board represents the highest CG mechanism that ensures the integrity of the financial reporting and builds trust between the management and shareholders.

Looking to the board composition, independent directors are more effective than inside directors in monitoring the management as they do not work for the companies. They are also more qualified and knowledgeable about financial issues and accounting practices (Beasley, 1996; Adams et al., 2010), are closer to shareholders and enjoy their trust as they look the independent directors to be good monitors (Fama and Jensen, 1983). In fact, independent directors are selected by the shareholders and thus they enjoy complete independence from the management.

Regulators highlight the importance of the presence of the independent members in the board. To this end, US regulations require that the independent directors should constitute the most of the board of listed firms (Security Exchange Commission (SEC), Governance Council, New York Stock Exchange (NYSE)). Saudi Arabia is similar to other countries in this respect. Specifically, Saudi CG guidelines issued by the Capital Market Authority (CMA) recommended that non-executive members should constitute the most of the board of directors, while, independent members should constitute one-third of the board of directors or not less than two members whichever is greater (CMA, 2006)[1.]

Studies on this issue have revealed that an independent board has a positive impact on the Financial Reporting Quality (FRQ), and in turn on the efficiency of the capital market (Beasley, 1996, Klein, 2002, Peasnell, Pope, and Young, 2005). For example, studies have documented that independent directors add value to the organization in terms of participating effectively in the board discussions (Klein, 2002), engaging in critical decisions such as dismissing the CEO (Weisbach, 1988), and being effectively involved in monitoring management acts (Alves, 2014).

The current study contends that the issue of the independent directors is even more important in Saudi Arabia. Looking at the business environment in Saudi Arabia, it is characterized by some of the factors that affect business structure and influence the financial reporting process.

For example, most Saudi firms are controlled by a few shareholders; these include family firms, and firms with block holders. In such type of firms, a few individuals own a large share of the firm and might use its resources for their own purposes; they might act opportunistically to maximize their own interest (Jensen and Meckling, 1976). In such cases, a higher divergence might exist between the controlling shareholders and the others who represent the numerical majority of the shareholders. This situation highlights the need to adopt an effective monitoring system to reduce conflicts and to enhance the quality of the reporting system. In fact, the independent board represents the core control mechanism that can help to enhance the FRQ (Beasley, 2005).

Meanwhile, the Saudi government has reported many corruption cases, both in the government and private sectors. In response to the increase in the number of corruption cases, in 2011 the government established a new organization for monitoring the corruption. It is the National Anti-Corruption Commission (NACC)[2]. The aim of the NACC is to monitor the administrative and financial corruption, including that related to financial reporting. It monitors

[1]CMA defines non-executive directors as members who do not have a position in the firm or work as employees; while, independent directors are board members who enjoy complete independence from management (CMA, 2006).
[2]It was established in 2011 under the name *Nazah*; the Arabic word means ‘anti-corruption’.

corruption in both government and joint projects with private sectors. In line with the new government movement against corruption and fraud, CMA has reported many of the biggest corporate accounting scandals in the Saudi stock market in recent years.

For example, Mobily[3], one of the biggest telecommunication firms in Saudi Arabia, was reported as a corrupt firm in 2013. The investigation in the Mobily case revealed that it had mis-accounted revenue related to the sale of top-up cards for handsets via third-party vendors leading to the under-reporting of revenue by 1.68 bn[4]. This event led to the suspension of its CEO for more investigation on his role in the accounting errors, a move that shocked not only the Saudi stock market but also GCC[5.] In fact, the Mobily case raises fears that other similar cases might exist in which a few people (either the CEO or top management) control the board of directors and direct it for their own benefit. The lessons learned from the Mobily case is the importance of improving FRQ through implementing effective CG mechanisms. One of these effective tools is the independent board.

Building on the above discussion, the aim of this study is to investigate the role of independent boards, which consist of the majority of the independent members, in improving the FRQ in Saudi nonfinancial listed firms.

The current study uses Ordinary Least Square (OLS) to test the relationship between the independent board and FRQ as measured by an abnormal accrual, proposing that the more independent a board is, the lower will be the level of abnormal accrual leading to higher FRQ. The earnings persistence is used as a proxy for FRQ in an additional test carried out to enhance the validity of this study. Moreover, an endogeneity test was conducted to test whether an independent board and abnormal accrual are simultaneously determined.

Using a sample of 417 observations of non-financial listed firms in Saudi during the period 2013- 2016, the current study found that the existence of an independent board is not related to improving FRQ. This result is consistent with the view that CG works differently in a business environment with structural and organizational biases, as can be observed in Saudi nonfinancial listed firms, many of which are, in fact, controlled by the CEO and top management.

This study contributes to the literature in terms of providing evidence on the role of independent boards inSaudi Arabia. Considering the environmental factors of emerging institutions, this study adds differing insights on the issue of the role of independent boards in FRQ. In practical terms, the study provides evidence on the new movement in Saudi Arabia toward anti-corruption that has begun to gather force in recent years.

The remainder of this paper is organized as follows: section two reviews the research literature on the issue; section three describes the methodology; section four reports the result; and finally, the summary and conclusion are presented in section five.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

In CG structure, the board of directors plays a vital role in monitoring financial reporting (Beasley, 1996; Fama and Jensen, 1983; Holtz and Neto, 2014; Vafeas, 2000). One of its responsibilities is the selection of external auditors who provide assurance on the reliability and relevance of financial reporting.

---

[3] Mobily is known as Etihad Etisalat in Saudi Stock market.
[4]For more details, see: www.ft.com/content/c186cf94-69cc-11e4-8f4f_00144feabdco.
[5] GCC is the Gulf Cooperation Countries including Saudi Arabia, Bahrain, Kuwait, Qatar, UAE, and Oman.

The board of directors also has the ultimate responsibility to ensure protecting the rights of shareholders. In this regard, directors might decide to fire CEOs whose actions are not aligned with the objective of firms (i.e. when they behave opportunistically to misuse the firm's resources). In this context, Saudi CG highlights the role of the board in reducing the conflict that might exist between management and shareholders. Specifically, it states that the board should ensure the integrity of financial reporting, develop a written policy that would regulate the relationship with shareholders, and review the effectiveness of internal control systems on an annual basis (CMA, 2006). On the other hand, it is suggested by the professional bodies that the board should be composed in its majority from independent directors (CMA, NYSE, SEC).

Prior studies have explored the role of independent boards on the FRQ and have revealed that a board composed of a majority of independent directors has a positive impact on the FRQ (Beasley, 1996, Klein,2002, Peasnell et al., 2005). Klein (2002) found that the independent board is associated with a reduction in the level of earnings management and in turn in higher FRQ. In this context, Peasnell et al. (2005) examined the role of outside board members in reducing the incidence of earnings management in UK firms. This study used abnormal accrual as a proxy of earnings management. They found that the likelihood of preventing the incidence of earnings management is related to the proportion of outsiders on the board. A recent study undertaken by Turegun (2018) examined the effect of independence of boards, among other factors, on the limitation of earnings management incidence in Turkish firms. The result of the OLS hypothesis testing revealed that a higher percentage of independent non-executive board members is important in reducing the level of earnings management, indicating that such members contribute positively to FRQ.

Summarizing, the independent board contributes to the financial reporting process in three main aspects: first, according to the market forces model, the value of independent directors is stated based on their experience and the extent of their knowledge and the benefit they add to the firms (Adams et al., 2010; Beasley, 1996; Famaand Jensen, 1983). In this regard, Hermalin and Weisbach (1988) argued that firms tend to nominate independent directors on the board because they are more qualified and knowledgeable and more able to express different ideas and opinions, which ultimately leads to achieving the objective of shareholders.

In short, firms use independent directors because they anticipate that independent directors are more efficient, and more familiar with the accounting reporting system than executive members. Thus, it is expected that independent directors will add value to the firms, as they are knowledgeable in the matters of monitoring financial reporting. Second, some studies have documented that independent directors are involved effectively in board decisions concerning the firms' CEOs, including nominating CEOs, approving their remunerations, or dismissing them if necessary (Alves, 2014; Famaand Jensen, 1983). This indicates that independent directors are positioned to prevent the opportunistic behaviour of management, thereby reducing the extent of financial reporting fraud. Third, independent directors are elected by shareholders primarily to carry out monitoring functions. Compared to executive directors, independent members neither work in the firms, nor receive any payment in the form of salary. As they are without any ties to the firms, they enjoy freedom from influence that might otherwise confound their work (Famaand Jensen, 1993). Thus, they can report faults of management without fear of any threat to their position in the firms. The studies of Chen, Cheng, Wang (2015), Duchin, Matsusaka, and Ozbas (2010), and Yermack (1996) provide evidence supporting this view.

In summary, independent directors gain the respect of shareholders who consider them to be good monitors and, moreover, experts in financial issues. As they work without any ties to management, they are freer to monitor the

management and in turn help enhance FRQ and protect shareholders' interests. Considering the new anti-corruption movement in Saudi Arabia that addresses the lack of a CG system, a discussion on the role of the independent board in improving FRQ is highly relevant.

Building on the above discussion, the current study examines the role of independent boards in improving FRQ; it proposes that as the number of independent board members increases, the effectiveness of the monitoring system increases, leading to a reduction in the level of abnormal accruals, and enhancing FRQ. Hence, the hypothesis of this study can be stated as follows: The independent board is positively related to FRQ of non-financial listed firms in Saudi.

METHODOLOGY

DATA

The sample includes all non-financial listed firms in Saudi TADAWL (i.e. the Saudi Stock Exchange) during the period 2013-2016. Data were obtained from the official site of TADAWL. As a one of listing requirements, every firm listed is required to present its financial report to TADAWL at the end of each year. Banks and insurance firms are excluded from the sample due to their unique control system (Chen et al., 2015; Holtz and Neto, 2014; Turegun, 2018). For using an abnormal accrual model, at least six observations in each industry should be available to run the regression model (De Fondand Jimbalvo, 1994). This led to the exclusion of energy and hotel firms from the sample. The TADAWL and Global Industry Classification Standard (GICS) are used to classify listed firms into eight different industry groups; namely Petrochemical, Cement, Retail, Agriculture, Multi-investment, Industrial investment, Building and Construction, and Real-estate development.

In total, the initial sample included 483 non-financial firms listed in the period covering 2013-2016. Three firms delisted in 2013 and 2016 and therefore they are excluded from the sample (12 observations in total); five firms with incomplete information are excluded(20 observations in total); energy and hotel firms(23 observations in total) are excluded due to the requirement to have a minimum of six observations for each industry included in the cross-sectional non-discretionary accrual model, as specified by De Fondand Jimbalvo (1994). Several outliers were detected, and they are also excluded from the sample (11 observations in total). With all these exclusions, the final sample consisted of 417 observations.

RESEARCH DESIGN

The current study uses OLS regression to test the hypothesis, while the logit regression model is also used as an additional test to address the issue of endogeneity. The independent variable of the study is the independent board. It is measured as a dummy variable, taken as 1 if the independent directors constitute the majority of the board directors, and 0 if otherwise. The independent directors are defined in line with the CMA definition as those board members who enjoy complete independence from management (CMA, 2006). FRQ is the dependent variable of this study. However, to alleviate any firm-specific heterogeneity issue that might affect the result, the regression model is estimated separately for each year. This yields four regression models that are used to test the study's hypothesis. Following prior studies (Davidson, Goodwin, and Kent, 2005; Klein, 2002), the current study uses abnormal accrual to measure FRQ, assuming that as the level of abnormal accrual decreases, the level of FRQ increases. An abnormal accrual is typically used as a proxy for earnings quality. A cross-sectional version of the modified Jones model is employed to estimate abnormal accrual. Under this model, total accrual is calculated as the sum of abnormal accrual and normal accrual (i.e. discretionary

accrual and non-discretionary accrual). Thus, abnormal accrual for a firm is calculated as estimated in equation 1:

$$AA_{ijt} = TAC_{ijt} - NA_{ijt} \qquad (1)$$

Where;

$$NA_{ijt} = \hat{\alpha}_j [1/A_{ijt-1}] + \hat{\beta}_{1j} [\Delta REV_{ijt} - \Delta REC_{ijt} / A_{ijt-1}] + \hat{\beta}_{2j} [PPE_{ijt} / A_{ijt-1}] \qquad (2)$$

Where $\hat{\alpha}_j$, $\hat{\beta}_{1j}$ and $\hat{\beta}_{2j}$ are industry-specific coefficients estimated from the following cross-sectional regression:

$$TAC_{ijt} / A_{ijt-1} = \alpha_j [1/A_{ijt-1}] + \beta_{1j} [\Delta REV_{ijt} / A_{ijt-1}] + \beta_{2j} [PPE_{ijt} / A_{ijt-1}] + \varepsilon_{ijt}$$

Where: TAC ijt is the total accruals for firm i in industry j in year t; AAijt is the abnormal accruals for firm i in industry j in year t; NA ijt is the normal accruals for firm i in industry j in year t; ΔREV ijt is the change in revenue for firm i in industry j between year t-1 and t; PPE ijt is the gross property, plant and equipment for firm i in year t; A ijt -1is the total assets for firm iin industry j at the end of the previous year; ΔREC ijt is the change in receivables for firm i in industry j between year t-1 and t.

A cash flow approach was used to predict the total accruals. This approach involves deducting the cash flow from operations obtained from the statements of cash flows, from the amount of net income (before extraordinary items) from the income statement (Davidson et al., 2005).

Earnings persistence is also used as a proxy of FRQ in an additional test to enhance the validity of the study. Notably, earnings persistence is used as a good indicator of subsequent earnings, assuming that current earnings can be used to anticipate future earnings, depending on the quality of financial statements. In other words, persistence is a useful attribute of the earnings quality providing that earnings truly reflect the current performance of the firm and continue smoothly in the following periods. In line with prior studies (Francis, LaFond, Olsson, Schipper, 2004; Larcker, Richardson, Tuna, 2007), this study measures persistence by using the negative slope coefficient estimate Q1 from an autoregressive model of annual split-adjusted Earnings Per Share (EPSit), measured as a firm’s financial statement net income before extraordinary items in year t divided by the weighted average number of outstanding shares during year t) as estimated in the following equation:

$$EPS_{it} = Q_0 + Q_1 EPS_{it-1} + V_{it}$$

Where, EPSit= earnings per share for the firm I at the end of year t; Vit=the residual

According to Francis et al. (2004), a value of Q1 approaching 1 implies that earning persistence is high; while, a value of Q0 approaching 0 implies highly transitory earning (i.e. earning persistence is low).

The control variables are developed in line with prior studies (Francis et al., 2004; Holtz and Neto, 2014; Larcker et al., 2007; Turegun, 2018) including board size, board meeting, loss, auditor quality, size, leverage, industry. Control variables are defined as follows: AA is the Abnormal Accrual calculated using the Jones cross-sectional model. Board Independence (BIND) is a dummy variable with the value of “1” when the board of directors has a majority of independent directors; firm size (SIZE) is the natural log of beginning year's asset. Leverage (LEV) is the ratio of total liabilities to total asset; audit quality(BIG4) is a dummy variable with the value of “1” when the auditor is a Big4 audit firm; loss(LOSS) is a dummy variable with the value of “1” when the firm reported a net income below zero and “0” otherwise; board size (BSIZE) is the total number of the board members; board meeting (BMEET) is the number of board meeting held during a

year; industry (INDUSTRY) is an Indicator variable taking the range from 1 to 8, industry classification used by The TADAWL and GICS. Models used in this study are as follows:

AA= f (Independent board, controls, e)

EPS= f (Independent board, controls, e)

RESULTS

As explained earlier, four models were used to test the hypothesis, each of which is tested for normality. The value of skewness and kurtosis revealed that all variables in the regression models fulfill the normality assumption, except the value of abnormal accrual in 2016. For this variable, data are transformed by using square root values, following which the data are re-tested to ensure that the variables are normally distributed according to normality assumption. The result shows that normality is achieved for all variables included in the regression models. Table 1 shows the results of the regression models. None of the coefficients of an independent board are significant, implying that an independent board is not related to FRQ, as measured by reducing the level of abnormal accrual (p=.55, .53, .24, .56 respectively).

Table 1: Regression Results

AA= β0+ β1BIND + β2SIZE + β3LEV+ + β4BIG4 + β5LOSS+ β6BSIZE + β7BMEET + β 8INDUSTRY + e				
Variables	**Model 1**	**Model 2**	**Model 3**	**Model 4**
Intercept	.00	.35	.00	.00
BIND	.55	.53	.24	.56
SIZE	.03*	.29	.02*	.26
LEV	.29	.97	.03*	.02*
BIG 4	.83	.66	.64	.66
LOSS	.98	.78	.26	.72
BSIZE	.34	.77	.64	.32
BMEET	.17	.50	.76	.12
INDUSTRY	.54	.00*	.69	.31

*p-values represent one-tailed tests when direction of coefficient is consistent with expectations; Variables are as defined in model specification in methodology section.

This result is in line with previous studies (Duchin et al., 2010; Chen et al., 2015) who found that independent boards are not effective in performing their monitoring role unless they are provided with low information acquisition cost. However, the result is inconsistent with those reported in other studies (Holtz and Neto, 2014; Peasnell et al., 2005; Turegun, 2018). The difference is attributable to agency theory. From an agency perspective, individuals are motivated by self-interest (Jensen and Meckling, 1976); hence, in a low CG situation, a small number of people who are in control (CEO and top management) might use their authority to maximize their own interest and make themselves better off by deviating from corporate objectives. This explains the increase of corruption cases, such as those reported for the Mobily firm. As a result, the lack of a CG system, like a weakness in the independence of the board as demonstrated in the current study, could lead to an increase in the level of abnormal accrual and, therefore, a reduction in the FRQ.

To probe further into the relationship between the presence of an independent board and FRQ, this study uses earnings persistence as an accounting measurement of FRQ. Table 2 summarizes the regression result for the earnings persistence model. The result indicates that board independence is not related to FRQ as measured by earnings persistence (p= .69). This finding is consistent with that revealed in abnormal accrual models. On the other hand, this further indication of lower CG quality in Saudi nonfinancial listed firms justifies calls to improve the legal system and the regulatory

environment in Saudi Arabia. The existence of new commission for anti-corruption is a notable step in the right direction.

Table 2: Regression Results for the Earnings Persistence Model

AA= β0+ β1BIND + β2SIZE+ β3LEV+ + β4BIG4+ β5LOSS + β6BSIZE + β7BMEET + β 8INDUSTRY + e					
Variables	**Exp Sign**	**B**	**VIF**	**t-Value**	**p-Value***
Intercept		.87		13.48	.00
BIND	+	.007	1.07	.40	.69
LEV	-	.09	1.05	2.04	.04*
BSIZE	+/-	.00	1.03	-.08	.93
BMEET	+	.01	1.02	2.82	.00*
INDUSTRY	?	-.03	1.02	-7.26	.00*

**p*-values represent one-tailed tests when direction of coefficient is consistent with expectations.
Adjusted R^2= 122
F-ratio = 12.62
Sig. *F*< 0.05

Variables are as defined in model specification in methodology section.

The current study also probes the possibility that an independent board and abnormal accrual are simultaneously determined, which might affect the validity of the result (Alves, 2014). To alleviate such concern, logit models are used to test whether the independent board is determined exogenously by abnormal accrual. Several control variables are included in the regression models as specified by prior studies (Alves, 2014; Chen et al., 2015; Duchin et al., 2010; Hermalin and Weisbach, 2003).

Table 3 shows that the coefficients of the abnormal accrual are not significant for the four logit models (p=.54, .51, .28, .69, respectively) implying that the study's findings are not biased by the endogeneity problem.

Table 3: Logit Model

BIND= AA + BIG4 + SIZE + LEV + BSIZE + LOSS + INDUS + e				
Variables	**Model 1**	**Model 2**	**Model 3**	**Model 4**
Intercept	.02*	.08**	.02*	.03*
AA	.54	.51	.28	.69
BIG4	1	.01*	.09	.98
SIZE	.63	.12	.01*	.04*
LEV	.03*	.92	.80	.06**
BSIZE	.02*	.91	.07	.35
LOSS	.17	.62	.72	.07**
INDUS	.10	.82	.20	.05**
Chi-square	18.3	9.9	7.5	10.4
Sig	.02	.27	.48	.24
Cox & Snell R^2	.185	.135	.17	.15

Note. *, ** Represent statistically significant at p<.05, p<.10 respectively

CONCLUSIONS

In a lower CG setting such as that of the Saudi stock market, which has experienced an increasing number of corruption cases in the recent years, the role of an independent board in improving FRQ has become a critical issue. From an agency perspective, a board with a majority of independent members is an important buttress to reduce the agency problem between the management and shareholders. In this regard, it plays a vital role in improving FRQ as it is effectively involved in critical decisions of the board such as nominating CEOs, approving their remunerations, and

dismissing them if necessary. Specifically, independent directors serving on the board are considered more qualified and knowledgeable about monitoring financial reporting, thus, they can contribute effectively to FRQ.

The current study examines the relationship between the independent board and FRQ. This study uses abnormal accrual to measure FRQ assuming that as the level of abnormality decreases, the quality of financial reporting increases. The modified Jones model is used to determine the abnormal accrual.

Using a sample of 417 observations from the non-financial listed firms in Saudi covering the period 2013 to 2016, the current study found that the presence of an independent board is not related to improve FRQ. This result is consistent with the view that CG works differently in a business environment with structural and organizational biases, specifically where firms are controlled by CEOs and top management.

However, the current study has some limitations. First, the independent board is defined based on secondary sources of data; namely the firm's own financial reporting. In fact, CMA uses a broad definition of what constitutes an independent board, and this opens the door to many interpretations of the concept. As a result, using the definitions included in firms' financial statements might be biased, since each firm has its own specific definition. Second, it is noted that some independent directors may leave the board, for any reason, before the end of the year and this may lead to miscalculations in the board composition, which could affect the accuracy of the study's result.

The current study also raises issues that might be explored further in future studies. While, this study uses abnormal accrual and earnings persistence to measure FRQ, it is suggested that future studies might use other measurements of FRQ, such as predictability, smoothness, value relevance, timeliness, and conservatism. On the other hand, since the current study uses a dummy variable to measure the presence (or absence) of an independent board, it is impossible to test the interaction of how that might impact the result. In this regard, it is suggested to test the interaction between board independence and other factors such as board meeting, board size, and the percentage of the insiders on the board.

REFERENCES

1. *Adams R., Hermalin., & Weisbach, M., (2010)," The role of Boards of Directors in Corporate Governance: A Conceptual Framework and Survey. Journal of Economic Literature, 48(1), 58-107.*
2. *Alves, S., (2014),"The Effect of Board Independence on the Earnings Quality: Evidence from Portuguese Listed Companies", Australasian Accounting, Business and Finance Journal, 8, 3, 23-44.*
3. *Beasley, M. S., (1996), "An Empirical Analysis of The Relation Between the Board of Director Composition and Fnancial Statement Fraud", The Accounting Review, 71 (4), 443–465.*
4. *Chen, X., Cheng, Q., Wang, X., (2015)," Does Increased Board Independence Reduce Earnings Management? Evidence from Recent Regulatory Reforms", Review Accounting Studies, 20, 899-933.*
5. *Davidson, R., Goodwin, J., & Kent, P., (2005)," Internal Governance Structures and Earnings Management", Accounting and Finance, 45, 241–267.*
6. *DeFond, M. L., and Jiambalvo. J., (1994), "Debt Covenant Violation and Manipulation of Accruals", Journal of Accounting and Economics, 17, 145-176.*

7. *Duchin, R., Matsusaka, J., and Ozbas, O., (2010)," When Are Outside Directors Effective?" Journal of Financial Economics, 96, 195-214.*

8. *Fama, E., & Jensen, M., (1983)," Separation of Ownership and Control", Journal of Law and Economics, 26(2), 301-325.*

9. *Francis, J., La Fond, R., Olsson, P., Schipper, K., (2004)" Costs of Equity and Earnings Attributes", The Accounting Review, 79(4), 967-1010.*

10. *Hermalin, B., and Weisbach, M., (1988)," The Determinants of Board Composition", Rand Journal of Economics, 4, 589-597.*

11. *Hermalin, B., and Weisbach, M., (2003)," Boards of Directors as An Endogenously Determined Institution: A Survey of The Economic literature", Economic Policy Review, 9(1), 7-26.*

12. *Holtz, L., and Neto, A, S., (2014), "Effects of Board of Directors' Characteristics on the Quality of Accounting Information in Brazil", R. Cont. Fin, 25(66), 255-266.*

13. *Jensen, M. C., (1993),"The Modern Industrial Revolution, Exit, and the Failure of Internal Control System", The Journal of Financial, XL VIII, 831-880.*

14. *Jensen, M. C., and Meckling, W. H., (1976),"Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure", Journal of Financial Economics, 3, 4, 305-60.*

15. *Klein, A., (2002)," Audit Committee, Board of Director Characteristics, and Earnings Management", Journal of Accounting and Economics, 33 (3), 375-400.*

16. *Larcker, D., Richardson, S., Tuna, I., (2007)," Corporate Governance, Accounting Outcomes, and Organizational Performance", The Accounting Review, 82(4), 963-1008.*

17. *Peasnell, K., Pope, P., and Young, S., (2005), "Board Monitoring and Earnings Management: Do Outside Directors Influence Abnormal Accruals?", Journal of Business Finance& Accounting,32 (7)& (8), 1311-1346.*

18. *Saudi Corporate Governance Regulation (2006), Available from:*

    http://www.cma.org.sa/En/Documents/CORPORATE%20GOVERNANCE.pdf

19. *Turegun, N., (2018)," Effects of Borrowing Costs, Firm Size, and Characteristics of Board of Directors on Earnings Management Types: A Study at Borsa Istanbul", Journal of Accounting & Economics, 25(1-2), 42-56.*

20. *Vafeas, N., (2000)," Board Structure and The Informativeness of Earnings", Journal of Accounting and Public Policy, 19, 139-160.*

21. *Weisbach, M. S., (1988)," Outside Directors and CEO Turnover", Journal of Financial Economics, 20, 431-460.*

22. *Yermack, D., (1996)," Higher Market Valuation of Companies with A Small Board of Directors", Journal of Financial Economics, 40, 185-211.*